(10)

No. 95-1340

IN THE
Supreme Court of the United States
OCTOBER TERM, 1996

HUGHES AIRCRAFT COMPANY,

Petitioner,

v.

UNITED STATES EX REL. WILLIAM J. SCHUMER,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF OF AEROSPACE INDUSTRIES ASSOCIATION OF AMERICA, INC. AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

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INTEREST OF THE AMICUS CURIAE

The Aerospace Industries Association of America, Inc. ("AIA") is a national, non-profit trade association representing manufacturers of commercial, military and business aircraft, helicopters, aircraft engines, missiles, spacecraft, and related components and equipment. AIA is comprised of fifty-one member companies, including many of the nation's largest corporations. Virtually all of AIA's members provide goods and services under contracts with the federal government, many deriving a significant portion of their business from such contracts.

Many of AIA's members who perform government contracts have been affected by the False Claims Act Amendments of 1986 ("1986 Amendments"), Pub. L. No. 99-562, 100 Stat. 3153, 31 U.S.C. §§ 3729, *et seq.* The 1986 Amendments stimulated a substantial increase in the number of *qui tam* actions brought by individuals (or "relators") empowered to bring actions in the name of the government against government contractors who are alleged to have submitted false claims to the government. Since 1986, AIA members have been named in over sixty such actions, including more than thirty *qui tam* actions.

Both petitioner and respondent have consented to the filing of this brief. Letters reflecting such consents have been filed with the Clerk of this Court.

SUMMARY OF ARGUMENT

This is a case in which petitioner Hughes Aircraft Company ("Hughes") used a contract cost-allocation method that saved the government money; the government conducted its own investigation in coming to that conclusion; and the government, in the course of its investigation, freely disclosed to others the allegations it was investigating. Yet, years after the investigation was concluded in Hughes' favor, the court below held that a former Hughes employee can proceed to trial against Hughes as a *qui tam* plaintiff under the False Claims Act ("FCA" or "the Act"), 31 U.S.C. §§ 3729 *et seq. United States ex rel. Schumer v. Hughes Aircraft*, 63 F.3d 1512 (9th Cir. 1995). A case more removed from the Act's purpose of assisting the government to ferret out fraud would be difficult to conjure.

The Ninth Circuit's holding that the 1986 Amendments apply retroactively disregards the principles laid down by this Court in *Landgraf v. USI Film Products*, 114 S.Ct. 1483 (1994).

Under the government-information test that determined the availability of private-plaintiff lawsuits before the 1986 Amendments, Hughes became effectively immune from a *qui tam* action when the government was advised of alleged irregularities in Hughes' accounting system, which had been in place long before the 1986 Amendments. Now, some ten years later, Hughes faces a *qui tam* trial because the Ninth Circuit, notwithstanding the palpable stakes in this case, concluded that the new law " 'did not change the legal consequences of' " Hughes' conduct. *Schumer*, 63 F.3d at 1517 (quoting *United States ex rel. Anderson v. Northern Telecom, Inc.*, 52 F.3d 810, 814 (9th Cir. 1995), *cert. denied*, 116 S.Ct. 700 (1996)). This was a misreading of *Landgraf*.

Landgraf reinforced the presumption against retroactive application of new laws where Congress has not explicitly required prospective application and where the law attaches new legal consequences to past conduct. Although the presumption does not apply to purely "jurisdictional" statutes, in the sense of laws that change the tribunal, this is because settled expectations about the legal consequences of one's conduct are not implicated by a mere change in tribunal. But it is the impact of a new law that controls, not its semantics. In seizing on the word "jurisdiction" in section 3730(e)(4)(A) of the Act, the Ninth Circuit favored the semantics, leading it to reverse the traditional presumption and apply new substantive law retroactively. *Landgraf* does not permit this result.

Its error on the retroactivity question caused the Ninth Circuit to apply the new public-disclosure test of the 1986 Amendments, 31 U.S.C. § 3730(e)(4)(A), in place of the government-information test. As relevant to this case, the public-disclosure test required determining whether there had been a public disclosure of allegations in an administrative investigation, where government investigators told various innocent employees of Hughes and another company, all of whom were

strangers to the fraud, about the allegations. *Schumer* found no public disclosure on the grounds that employees of a company under investigation cannot be considered members of the public. This broad conclusion rested on the court's view that the economic incentives facing employees are too strong to "trigger the potential for corrective action" under the Act. *Schumer*, 63 F.3d at 1518. As additional support, *Schumer* announced that "the government, contractors, and subcontractors operate within a closed loop of secrecy," *id.*, so that all discussions among them must be deemed private. The court's disposition thus rested, essentially, upon psychological and sociological conclusions.

The False Claims Act does not endorse this loose approach. The Act nowhere suggests that the government cannot make a public disclosure to the employees of a company under investigation or to employees of other companies. Generalization about how an audience might react after hearing fraud allegations — keeping them confidential, disclosing them, or filing a *qui tam* lawsuit — do not illuminate their public or private character.

Nor does the Act sanction any special rule for the defense-procurement industry. Congress made no finding that unrestricted government disclosures about a fraud investigation to a defense contractor's employees constitute sensitive security information or are otherwise private in any way. The Ninth Circuit's generalization on this score has no greater support in the Act or its legislative history than its preconceptions about employees' willingness to sue their employers.

Congress fully recognized the special role of company employees as potential *qui tam* plaintiffs when it amended the Act in 1986, providing special statutory protections for employees who blow the whistle, including employees in the defense-procurement industry. More broadly, the structure

and text of the Act reveal Congress' latest attempt to balance competing concerns about how to encourage some *qui tam* suits while forbidding others. Using the concept of "public disclosure" to tip the balance is not the courts' function. Rather, creating exceptions for employees, defense contractors, or any other group, based on a court's subjective view of whether the allegations are more or less likely to be acted upon, simply rewrites the Act. The public disclosure that occurred in this case should have ended the lawsuit, even under the mistaken application of current substantive law.

ARGUMENT

A. The Public-Disclosure Test of the False Claims Act Can Apply Only Prospectively.

In *Landgraf v. USI Film Products*, 114 S.Ct. 1483 (1994), the Court crystallized the extensive jurisprudence governing whether a new law may be applied retroactively absent explicit legislative direction requiring that result.[1] *Landgraf* clarifies that "prospectivity remains the appropriate default rule," thus confirming "the well-settled presumption against application of the class of new statutes that would have genuinely 'retroactive' effect," *id.* at 1501, 1503. As the Court phrased the test, whether a new statutory provision has genuinely retroactive effect depends upon whether it

[1]There has been no suggestion in this case that any express statement or clear congressional intent favors retroactive application of section 3730(e)(4)(A). *See also Hyatt v. Northrop Corp.*, 80 F.3d 1425, 1428 (9th Cir. 1996) ("Congress has not expressly indicated whether the 1986 amendments to the FCA apply retrospectively . . . ."), *petition for cert. filed*, No. 96-17 (Jul. 2, 1996); *Schumer*, 63 F.3d at 1517 ("Congress did not demonstrate an intent that the FCA should apply retrospectively.") (citations omitted).

> would impair rights a party possessed when he acted, increase a party's liability for past conduct, or impose new duties with respect to transactions already completed.

Id. at 1505. In brief, a law has impermissible retroactive effect if it "attaches new legal consequences to events completed before its enactment." *Id.* at 1499.[2] If so, it "does not govern absent clear congressional intent favoring such a result." *Id.* at 1505.

Exposing FCA defendants to a cause of action from a large and indeterminate number of potential *qui tam* plaintiffs, which is precisely the effect of section 3730(e)(4)(A), "increase[s] a party's liability for past conduct" and "attaches new legal consequences" to past events within the meaning of *Landgraf*. The unfairness inherent in any retroactive operation of laws is intensified in this case because elimination of the government-information test upsets legitimate expectations and frustrates planning. Under the government-information test, a defendant could foreclose all *qui tam* lawsuits by engaging in certain specific and appropriate conduct: disclosing to the government the allegations of fraud. The new law eliminated the legal benefit flowing from that ameliorative conduct and extracted a new price — effecting a "public disclosure" — for limiting the number of potential *qui tam* plaintiffs who might bring the suit. In this sense, the new law

[2]*Landgraf* cited approvingly several other formulations of the test from previous cases and commentary. Thus, a law operates retroactively, and can be applied only prospectively, if it "changes the legal consequences of acts completed before its effective date," *Weaver v. Graham*, 450 U.S. 24, 31 (1981); gives "a quality or effect to acts or conduct which they did not have or did not contemplate when they were performed," *Union Pacific R.R. Co. v. Laramie Stock Yards*, 231 U.S. 190, 199 (1913); or "operate[s] on transactions which have occurred or rights and obligations which existed before passage of the act," 2 N. Singer, Sutherland on Statutory Construction § 41.01, p. 337 (5th rev. ed. 1993).

"impair[s] rights a party possessed when he acted" and "impose[s] new duties with respect to transactions already completed." *Id.* The "well-settled presumption" against retroactive application of laws must operate in this case.

1. The 1986 Amendments Expanded Defendants' Exposure to *Qui Tam* Lawsuits.

Under the government-information test prior to the 1986 Amendments, parties who were alleged to have committed fraud were completely free from *qui tam* lawsuits "when 'the action [was] based on evidence or information the Government had when the action was brought.' 31 U.S.C. § 3730(b)(4)(1982)." *Hyatt*, 80 F.3d at 1428. Under the public-disclosure test of current law, the very same conduct is subject to a *qui tam* lawsuit, by original sources or others, even if the government already has the information.[3] That the change in the law greatly expanded the circumstances under which allegedly fraudulent conduct would be subject to a *qui tam* lawsuit is unassailable. *See, e.g., United States v. TRW, Inc.*, 4 F.3d 417, 422 (6th Cir. 1993) ("The amendments expand the circumstances under which citizens may bring false claims suits . . . ."), *cert. denied sub nom. Eagleye v. TRW, Inc.*, 114 S.Ct. 1370 (1994); *United States ex rel. Kreindler v. United Technologies Corp.*, 985 F.2d 1148, 1153 (2nd Cir. 1993) ("Congress . . . create[d] a legal interest and confer[red] stand-

[3]The 1986 Amendments provided that

> No court shall have jurisdiction over an action under [the section on civil actions under the FCA] based upon the public disclosure of allegations or transactions in a criminal, civil, or administrative hearing, in a congressional, administrative, or Government Accounting Office report, hearing, audit, or investigation, or from the news media, unless the action is brought by the Attorney General or the person bringing the action is an original source of the information.

31 U.S.C. §3730(e)(4)(A).

ing to assert it."), *cert. denied*, 508 U.S. 973 (1993); *United States ex rel. LeBlanc v. Raytheon Co.*, 913 F.2d 17, 19 (1st Cir. 1990) ("Basically, Congress broadened the universe of potential plaintiffs . . . ."), *cert. denied*, 499 U.S. 921 (1991).

The fact that a new statute encompasses conduct previously prohibited or subject to monetary liability is not dispositive of whether it changes the legal consequences of past conduct. The Court in *Maitland v. University of Minnesota*, 43 F.3d 357 (8th Cir. 1994), correctly rejected the argument that "[s]ubstantive changes . . . are [only] 'those which make illegal conduct which was legal before the change in the law,' " stating that this formulation "defines a substantive change too narrowly and in a manner inconsistent with the Supreme Court's definition of true retroactive effect as set out in *Landgraf*." *Id.* at 362. Nor is a statutory increase in direct financial penalties required. Permitting, barring, or resurrecting causes of action are "legal consequences." *Landgraf*, 114 S.Ct. at 1506 ("§ 102 can be seen as creating a new cause of action . . . ."); *Million v. Frank*, 47 F.3d 385, 390 (10th Cir. 1995) (forcing the defendant to defend a cause of action previously time-barred substantially increases defendant's liability). To say that the "extent of a party's liability . . . cannot be ignored," *Landgraf*, 114 S.Ct. at 1507, is not to say that all other legal consequences *can* be ignored.

Whereas FCA defendants were formerly liable to suit only by the government in cases where the government had the information, the law now encourages any number of *qui tam* plaintiffs to be the first to sue even if the government chooses not to proceed, as happened in this case. Potential liability to party A (the government) for allegedly wrongful conduct is certainly a legal consequence. Potential liability also to parties B, C, or D . . . (*qui tam* plaintiffs) for the same conduct is obviously a more dire legal consequence. In this case, where the

government chose not to sue because it had not been harmed (but actually benefited), the difference is between exoneration and protracted litigation. But in any case, unless reality is ignored, adding to the litigants potentially arrayed against a party increases that party's legal liability.[4]

While the change in the law did not alter the underlying obligation not to commit fraud, *see United States ex rel. Lindenthal v. General Dynamics Corp.*, 61 F.3d 1402, 1408 (9th Cir. 1995), *cert. denied sub nom. United States ex rel. Willis v. General Dynamics Corp.*, 116 S.Ct. 1319 (1996), it did substantially alter the legal effect of that conduct. Worse yet, however, it altered the legal effect of innocent conduct, because both the government-information test and the public-disclosure test are keyed to the mere lodging of fraud allegations. Therefore, whether the target is culpable or innocent, "the law imposes additional burdens based on conduct that occurred in the past." *Landgraf*, 114 S.Ct. at 1506 n. 35.

2. The 1986 Amendments Curtailed Defendants' Ability to Take Remedial Action Reducing Their Liability.

The change wrought by section 3730(e)(4)(A) not only increased FCA defendants' legal burden substantially, it constituted "the type of legal change that would have an impact on private parties' planning." *Id.* at 1506. Under the government-information test, a company that learned of fraud or possible fraud by one of its employees could completely eliminate the threat of any *qui tam* lawsuit by itself informing the

[4]The threat of suit from additional quarters clearly constitutes an increase in "liability." According to Black's Law Dictionary, "The word is a broad legal term . . . . It has been referred to as of the most comprehensive significance, including almost every character of hazard or responsibility, absolute, contingent, or likely." *Black's Law Dictionary* 823 (5th ed. 1988).

government of the allegations.[5] The decision to advise the government of one's own possible fraud is not made lightly: at a minimum, it brings an investigation, internal company strife, the likelihood of negative publicity, probable disruption of other government contracts, and the risk of adverse findings even if the company is innocent.[6] Certainly the guilty, but perhaps especially the innocent, have strong incentives to remain silent in the face of allegations of often uncertain validity.

Yet the ability to eliminate *qui tam* actions is a powerful counter-incentive. A company that believed the allegations were spurious might conclude that full disclosure to the government would permit vindication without litigation, with minimal publicity, and with a relatively prompt return to normalcy, all of which would likely compare favorably to a federal-court lawsuit by a *qui tam* plaintiff induced by the prospect of an enormous recovery. Even companies who discover true fraud within their ranks might rationally prefer dealing with dispassionate, experienced government investigators, more likely than financially motivated *qui tam* plaintiffs to place the wrongdoing in proper perspective, administer an appropriate sanction, and put the matter in the past.

When it adopted the public-disclosure test, Congress removed these incentives entirely. A company's conduct could no longer eliminate the threat of a *qui tam* lawsuit and only by making a

[5]In *Anderson*, 52 F.3d at 814, the court overlooked this critical point in stating, "If Northern Telecom really did submit a fraudulent claim, it became liable and remained liable to the government *and* to potential *qui tam* relators." (Emphasis added). Under prior law, if the government had the information no *qui tam* action would lie.

[6]This case shows that mistakes can be made. The government's initial investigation caused it to withhold $15.4 million from Hughes, a penalty it reversed much later. It is the proverbial "uncertainties of litigation," and its expense, that constitute adverse legal consequences even to innocent defendants. *Schumer*, 63 F.3d at 1516.

public disclosure of the allegations could the alleged wrongdoer limit the category of possible *qui tam* plaintiffs, *i.e.*, to those who qualify as an "original source." In short, in many cases, the new law extracts a far dearer price to obtain far less protection from liability in a *qui tam* lawsuit.

In an analogous context, *Landgraf* deemed it significant that notice of the new law could have influenced a defendant's conduct:

> The new damages provisions of § 102 can be expected to give managers an added incentive to take preventive measures to ward off discriminatory conduct by subordinates *before* it occurs, but that purpose is not served by applying the regime to preenactment conduct.

Landgraf, 114 S.Ct. at 1506 n. 35 (emphasis in original). Likewise, the new law in this case removed a significant incentive for potential FCA defendants to disclose allegations of fraud promptly to the government. *See, e.g., TRW, Inc.*, 4 F.3d at 419 (defendant informed government of internal investigation revealing accounting irregularities). Whether a company commits fraud does not likely hinge on the availability *vel non* of *qui tam* lawsuits; whether a company *reports allegations of fraud* may well depend on that factor. Certainly the target's conduct — silence, informing the government, or making a public disclosure — is directly relevant to the remedial purposes of the Act.[7] Under these circumstances, changing the legal

[7]"One theme recurring through the legislative history in 1985 is the intent to encourage persons with first-hand knowledge of fraudulent misconduct to report fraud." *United States ex rel. Stinson v. Prudential Insurance Co.*, 944 F.2d 1149, 1154 (3rd Cir. 1991). This was to include "individuals who are either close observers or otherwise involved in the fraudulent activity." *Id.* (citation omitted). *See also Wang. v. FMC Corp.*, 975 F.2d 1412, 1419 (9th Cir. 1992) ("*Qui tam* suits are meant to encourage insiders privy to a fraud on the government to blow the whistle on the crime.").

consequences of the allegedly wrongful conduct cannot be given retroactive application.

3. Section 3730(e)(4)(A) Is Not "Jurisdictional" for Purposes of Retroactive Application.

Landgraf's extensive analysis of the principles governing the retroactivity of legislation recognized that, notwithstanding "a *presumption* against retroactivity . . . , application of new statutes passed after the events in suit is unquestionably proper in many situations." *Landgraf*, 114 S.Ct. at 1501 (emphasis in original). One such situation concerns "intervening statutes conferring or ousting jurisdiction, whether or not jurisdiction lay when the underlying conduct occurred or when the suit was filed." *Id.*

But *Landgraf* did not hold that every statutory provision that may be couched in jurisdictional terms is presumed to apply retroactively. The Court's explanation was considerably more refined:

> Application of a new jurisdictional rule *usually* "takes away no substantive right but *simply changes the tribunal* that is to hear the case." Present law *normally* governs in such situations because jurisdictional statutes "speak to the power of the court *rather than to the rights or obligations of the parties* . . . ."

Id. at 1502 (emphasis added) (citations omitted). Indeed, in the seminal case embodying the "jurisdictional rule," *Bruner v. United States*, 343 U.S. 112, 117 n.8 (1952), the Court pointedly stated:

> This jurisdictional rule does not affect the general principle that a statute is not to be given retroactive effect unless such construction is required by explicit language or by necessary implication.

Schumer thus misstated the analysis when it said: "The *Landgraf* Court, however, carved out an exception to that rule [presuming only prospective application] in the case of jurisdictional statutes." *Schumer*, 63 F.3d at 1517. Retroactive *application* of jurisdictional laws is not an exception to the ban on retroactive *operation* of substantive rules. It is only because true jurisdictional statutes do not attach new legal consequences to past conduct — they do not change the substantive law — that they are applied retroactively. When a new statute has a genuine retroactive effect because it changes substantive law, labeling it "jurisdictional" shifts no presumptions.[8]

In noting that jurisdictional statutes *usually* only "change the tribunal that is to hear the case" and *normally* do not speak to "the rights or obligations of the parties," *Landgraf*, 114 S.Ct at 1502 (citation omitted), *Landgraf* left room for provisions that sound in jurisdiction but have nothing to do with changing tribunals and everything to do with parties' substantive rights. Such is section 3730(e)(4)(A), which did not change tribunals, but rather *limited* the circumstances under which *no* court shall have jurisdiction, thereby providing additional persons with a *qui tam* cause of action. Courts have readily acknowledged this as a sweeping substantive change. *See, e.g., Anderson*, 52 F.3d at 813 ("an entirely new scheme"); *TRW, Inc.*, 4 F.3d at 422 (expanding the circumstances for citizen suits); *Kreindler*, 985 F.2d at 1153 (creating new legal interests); *LeBlanc*, 913 F.2d at 19 (broadening the universe of potential plaintiffs).

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[8]The confusion surrounding the phrase "jurisdictional bar" is illustrated in *Stinson*, 944 F.2d at 1152, n.1. The court characterized 31 U.S.C. § 3730(e)(3), which forecloses certain *qui tam* actions where the government is a party, as a "jurisdictional bar" even though the provision does not contain the word "jurisdiction" and has nothing to do with where a case can be heard. Just as subsection (e)(3) is not jurisdictional, subsection (e)(4), which operates in identical fashion to bar other *qui tam* actions, is not either.

The new public-disclosure test is thus a different legal animal from the jurisdictional provisions in *Bruner* and other cases, which involve only changes in which tribunal has power to hear a case. *See Bruner*, 343 U.S. 112 (jurisdiction in Court of Claims or district court); *Hallowell v. Commons*, 239 U.S. 506 (1916) (jurisdiction in Secretary of Interior or district court); *Assessor v. Osbornes*, 76 U.S. (9 Wall.) 748 (1870) (jurisdiction in state court or circuit court); *Andrus v. Charlestone Stone Products Co.*, 436 U.S. 604 (1978) (jurisdiction in federal court or state court); *Smallwood v. Gallardo*, 275 U.S. 56 (1927) (jurisdiction in Puerto Rico or federal court). *Landgraf's* careful explanation accommodates this difference; *Schumer* did not.

Accordingly, there is no reason to reverse the presumption in this case. As stated in *United States ex rel. Fallon v. Accudyne Corp.*, " 'Jurisdiction' is a notoriously plastic term.":

> For what it is worth, we doubt that § 3730(e)(4)(A) uses the word "jurisdiction" in the sense of adjudicatory power, which is conferred by §§ 1331, 1345, and 3732(a) rather than "this section" (sec. 3730). In context, the word appears to mean that once information becomes public, only the Attorney General and a relator who is an "original source" of the information may represent the United States. This does not curtail the categories of disputes that may be resolved (a real "jurisdictional" limit) but instead determines who may speak for the United States on a subject, and who if anyone gets a financial reward. "Jurisdiction" is a notoriously plastic term.

97 F.3d 937, 941 (7th Cir. 1996). Because section 3730(e)(4)(A) effects a major change in substantive law, its use of the word "jurisdiction" is of no moment and "prospectivity remains the appropriate default rule" in this case. *Landgraf*, 114 S.Ct. at 1501.

B. There Was A Public Disclosure In This Case.

In this case, it is undisputed that the government disclosed the allegations of fraud to various individuals who were either employees of Hughes, the target company, or employees of Northrop, which had a contract with Hughes and which alerted the government to Hughes' alleged accounting irregularities. None of these employees was suspected of being involved in the alleged fraud. As far as appears in the opinion, none of them was advised that the information disclosed to them was secret, confidential, or "nonpublic" in any way. Yet *Schumer* held that no "public disclosure" could have occurred because these strangers to the fraud happened to be employees of one or the other company. The court added its opinion that the government and defense contractors inherently operate in secret. *Schumer*, 63 F.3d at 1518-19.

Schumer's holding rests not on the text of the False Claims Act, but on the court's belief that the purposes of the Act would be best served by an across-the-board rule that disclosures to employees are not public. Without questioning Hughes' claim that there was an unrestricted disclosure, the court nonetheless deemed the information to have been " 'disclosed in private.' " *Id.* (citation omitted). This characterization had nothing to do with the nature of the information, the number of recipients, any known caution or advice on further dissemination, or any other specific indicia of confidentiality. It was simply the court's judgment that employees of the defendant company and its subcontractor are not " 'members of the public' to whom 'public disclosure' can occur." *Id.* (citation omitted).

Schumer's gloss on section 3730(e)(4)(A) contrasts with the Second Circuit's straightforward reading in *United States ex rel. Doe v. John Doe Corp.*, 960 F.2d 318, 323 (2d Cir. 1992), holding that "[o]nce allegations of fraud are revealed to mem-

bers of the public with no prior knowledge thereof, the government can no longer throw a cloak of secrecy around the allegations . . . ."[9] Eschewing *Doe*'s neutral reading, *Schumer* adopted the *Doe* dissent, putting employees into a special category:

> We decline to adopt the rule of *Doe* for application in this circuit. At one level, the *Doe* court's treatment of company employees as members of the public is unrealistic. Unlike others who come across information related to fraud, an "innocent employee who comes forward with allegations of fraud by her employer knows that her job may be in jeopardy." *Doe*, 960 F.2d at 325 (Walker, J. dissenting). *Because the employee has a strong economic incentive to protect the information from outsiders, revelation of information to an employee does not trigger the potential for corrective action presented by other forms of disclosure.* Because disclosure of such allegations could reflect negatively on both Northrop and Hughes, this reasoning applies to employees of both companies.

Schumer, 63 F.3d at 1518 (emphasis added).

Schumer then applied equally broad reasoning to the defense procurement industry:

> Indeed, this circuit has indicated that disclosure by one government employee to another would not constitute public disclosure. *See United States ex rel. Hagood v. Sonoma County Water Agency*, 929 F.2d 1416, 1419 (9th Cir. 1991). Yet *in the context of defense procurement, security considerations generally require that the government, contractors, and subcontractors operate within a closed loop of secrecy.* We see no principled distinction between disclosure to other government employees and to employees of defense contractors and subcontractors. Both situations involve the release of information within a private sphere.

[9] *Doe* made an explicit finding that "[w]hen these innocent employees learned of the fraud, they were under no obligation to keep this information confidential." *Doe*, 960 F.2d at 323. *Schumer* obviously found this fact, which appears to be present in this case as well, irrelevant to its analysis.

Id. (emphasis added).

This second sweeping assessment, this time characterizing the defense industry, creates doubt about *Schumer*'s intended reach. At one level, *Schumer* holds that when the government shares fraud allegations with a target company's employees and employees of companies somehow related to the subject matter, there is no public disclosure. A narrower reading would restrict this holding to employees (of either company) if they are in the defense procurement industry. But both readings depend on the court's view of what the Act should have said, not what it says.

1. There Is No Exception for Employees.

Schumer makes a blanket finding that company employees will not blow the whistle on their employers: "Because the employee has a strong economic incentive to protect the information from outsiders, revelation of information to an employee does not trigger the potential for corrective action presented by other forms of disclosure." *Id.*

This is a remarkable statement. Three years before it decided *Schumer*, the Ninth Circuit acknowledged that "[t]he paradigm *qui tam* plaintiff is the 'whistleblowing insider.' "

Wang, 978 F.2d at 1419 (citation omitted). *Wang* quoted the Third Circuit in *Stinson*, which viewed company employees as the primary source of *qui tam* litigants:

> The paradigmatic "original source" is a whistleblowing insider. This covers those the Senate Report specifically referred to: "individuals who are close observers or otherwise involved in the fraudulent activity." S. Rep. No. 345, at 4, reprinted in U.S. Code Cong. & Admin. News 5269. *Other relators may also qualify* if their information results from their own investigations.

Stinson, 944 F.2d at 1161 (emphasis added).

The Ninth Circuit's recognition that Congress expected company employees to comprise an important source of *qui tam* plaintiffs begs the question why, according to *Schumer*, Congress failed to provide adequate incentives for employees to come forward. The answer is that Congress provided the incentives and protections it saw fit, including specific protections for company employees. *Schumer* simply usurps that legislative prerogative.

It does so on the assumption, indistinguishable from a legislative judgment, that employees have insufficient incentive to become whistleblowers. Indeed, soon after it rendered *Schumer*, the Ninth Circuit again offered its view of the appropriate inducement for employees to file *qui tam* actions:

> Recall, in this light, that the False Claims Act provides a statutory fine of between \$5,000 and \$10,000 for every false claim submitted to the government, as well as triple compensatory damages. The relator is entitled to share in as much as 30% of the settlement or judgment depending on whether the United States intervenes in the action. Thus, potential recoveries for qui tam relators are staggeringly large, as well they should be for insiders in private companies who risk their jobs and reputations when they blow the whistle on their own employers.

United States ex rel. Fine v. Chevron, U.S.A., Inc., 72 F.3d 740, 743-44, n.3 (9th Cir. 1995), *cert. denied*, 116 S.Ct. 1877 (1996). The Ninth Circuit apparently believes that even "staggeringly large" potential recoveries are inadequate incentive for employees to bring fraud to light. *Schumer*, 63 F.3d at 1518. Accordingly, as *Schumer*'s reasoning goes, the government's unrestricted release of fraud allegations to employees have "not been publicly disclosed." *Id.*

This redraft of the Act contradicts Congress's specific consideration of how to foster *qui tam* lawsuits by employees. As noted in a Ninth Circuit opinion rendered some eight months after *Schumer*,

> Prior to 1986, the FCA did not contain any provision for the protection of discharged employees. However, the 1986 amendments to the FCA included the addition of a discharged employee protection provision. This provision states:
>
> > Any employee who is discharged, demoted, suspended, threatened, harassed, or in any other manner discriminated against in the terms and conditions of employment by his or her employer because of lawful acts done by the employee on behalf of the employee or others in furtherance of an action under [the FCA] . . . shall be entitled to all relief necessary to make the employee whole.
>
> 31 U.S.C. § 3730(h).

Hyatt, 80 F.3d at 1430. *Schumer* concludes that these additional protections are still inadequate, justifying its gloss on "public disclosure." But where Congress directly addressed employees' "economic incentive to protect the information from outsiders," *Schumer*, 63 F.3d at 1518, courts must respect that legislative judgment.

Schumer's failure to do so led it to speculate about the fears and motivations of an entire group of *qui tam* plaintiffs in determining whether the disclosure is likely to "trigger the potential for corrective action." *Id.* Indeed, the dissent in *Doe*, which *Schumer* adopted at least in part, *id.*, candidly called for a plaintiff-by-plaintiff prediction of future conduct:

> I do not agree that advising individual employees of the targeted organization would *necessarily* constitute a public disclosure under the statute . . . . Thus, in assessing whether or not there has been a public disclosure, courts should be focusing on whether there has been a sufficient dissemination such that it is reasonably likely that the fraud will come to light . . . . [T]here *might be* a public disclosure where the fraud is privately disclosed to people with an incentive to bring the fraud to public attention. However, I think it unlikely that this standard would be met *in the present case* . . . .

960 F.2d at 324-25 (Walker, J., dissenting) (emphasis added).

It is unclear whether *Schumer* endorses the plaintiff-by-plaintiff approach or only the group approach,[10] but each poses intractable problems. An exception for company employees, while simple enough to apply, ignores the diverse motives

[10]*Schumer*'s inclusion of Northrop's employees in its reasoning, even though Northrop initiated the government investigation, at least makes it clear that its holding is not limited to target-company employees.

among employees, many of whom have proven quite willing to file *qui tam* suits. Employees of non-target companies are even harder to characterize, with the employee seeing himself as hero or outcast — "insider" or "outsider" — depending on the circumstances. Adjudication by stereotype is inherently flawed.

The same morass surrounds other groups. Companies and individuals in various positions have varying economic stakes in the fortunes of those with whom they transact business. For example, a given supplier may be highly dependent on a large customer who becomes the object of fraud allegations, providing a strong incentive not to blow the whistle. Yet a disgruntled supplier — or employee, or customer, or competitor, *ad infinitum* — may leap at the chance even absent a potential *qui tam* recovery. The relevant motivations and perceptions of interest will change constantly with the myriad circumstances that influence relationships between companies and the personalities involved. In short, this is exceedingly slippery terrain.

The litigant-by-litigant approach is not an improvement. Prospective and retired employees, who may be just as likely as current employees to become privy to government investigations, also have unique and variable incentives. Cases will arise where disclosures are made simultaneously to employees and non-employees, or to employees of companies who would not be tainted, but rather exonerated, by the allegations. Or the plaintiff's conduct may belie the stereotype — perhaps the employee who receives the information does not keep it secret, but feeds it to the rumor mill, *or files a qui tam action.*[11]

[11]*Schumer* does not state how it would handle the public disclosure issue when the company employee actually files the *qui tam* suit, given its broad conclusion that "treatment of company employees as members of the public is unrealistic." *Schumer* 63 F.3d at 1518.

The omnipresent pressure to protect company secrets, so certain and significant in *Schumer*, in reality varies with each employee's compensation, personal financial needs, job satisfaction, moral code, and innumerable other elusive factors.[12] The Ninth Circuit's approach, insofar as it approves the dissent in *Doe*, would have courts reading minds in order to determine who is likely to keep a secret.

2. There Is No Exception for the Defense Procurement Industry.

Claiming it to be a " 'practical, commonsense interpretation' " of section 3730(e)(4)(A), *Schumer* holds that government disclosures to "employees of defense contractors and subcontractors" are not public disclosures. *Schumer*, 63 F.3d at 1518 (quoting *Stinson*, 944 F.2d at 1161). This holding rests on the court's observation that, "in the context of defense procurement, security considerations generally require that the government, contractors, and subcontractors operate within a closed loop of secrecy." *Id.*

This was an especially odd case for relying on generalities, because *Schumer*'s factual predicate was that the material the government disclosed was ***not*** classified. *Id.* (recounting Hughes' allegation "that Schumer's action is barred because it is based upon ***unclassified*** government audits which have been disclosed publicly" (emphasis added)). Without disputing Hughes' characterization, *Schumer* simply relied on what "security considerations generally require." *Id.* Yet this very case belies the general rule.

Nor is *Schumer* unique in presenting a *qui tam* action against a defense contractor where national security or other government secrets played no part in the case. *See, e.g., Hyatt*, 80 F.3d at 1429 (complaint not filed under seal); *Lindenthal*, 61 F.3d 1402 (no mention of government secrets or national security)[13]; *TRW, Inc.*, 4 F.3d at 420 (allegations appeared in the news media); *Kreindler*, 985 F.2d at 1158 (information "available to anyone who wished to consult the court file"); *Wang*, 975 F.2d at 1417 (allegations discussed in newspaper accounts); *Doe*, 960 F.2d at 322 ("allegations of fraud . . . divulged to strangers to the fraud"); *LeBlanc*, 913 F.2d 17 (no mention of government secrets or national security).

[12]One such factor, of course, is whether the employee or other recipient even perceives the information as secret, especially where the government freely discloses it without restriction.

Cases may arise where government security considerations prevent the public disclosure of fraud allegations. Other cases may involve obvious public disclosures notwithstanding security restrictions. In any case, however, the issue is whether a public disclosure occurred, not whether an industry or setting is "generally" characterized by secrecy. *Schumer*'s holding that public disclosures simply do not occur in the government-defense contractor setting, or occur so rarely that courts need take no account of them, ignores the almost daily fare of the nation's newspapers.

Beyond its misapprehension about defense contracting, *Schumer*'s fundamental error is its value-laden approach to interpreting statutory terms based on speculation about the purposes of the Act. *Schumer*'s attempt to foster more *qui tam* suits even though the government already has the information and discloses it to others, 63 F.3d at 1518-19, led it to create broad categories of "public" and "private" disclosure that have no support in the text, structure, or legislative history of the 1986 Amendments. If Congress had employed such

[13]*Lindenthal* involved a few documents that were found to be either internal company memoranda or private correspondence between the company and the government. Although they were held not to have been publicly disclosed, nothing about any national security or government secrets was mentioned in the opinion.

generalizations, inaccurate though they might be, at least it would be the legislature doing the legislating, rather than individual courts attempting to promote one or another competing purpose of the Act.[14]

In any event, *Schumer*'s belief that its holding is necessary "to avoid total reliance on government enforcement," *id.* at 1519, is wrong: the 1986 Amendments permit original sources to become *qui tam* plaintiffs even if the government has the information and even if there has been a public disclosure. Although certain parasitic *qui tam* actions will be foreclosed, original-source lawsuits will not. Perhaps most importantly, even if no *qui tam* suit is filed, the government cannot shroud the allegations in secrecy, sitting on the fraud without public scrutiny, once it abandons exclusive knowledge of them by disclosing them to strangers to the fraud. The text and structure of section 3730(e)(4)(A) reveal this to be the balance that Congress struck. The courts must respect it.

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[14]As the Fourth Circuit has stated:

> [A]lthough we can perhaps divine from these abstract purposes a congressional intention to balance the need to encourage qui tam actions against the need to prevent parasitic suits, we can discern virtually nothing as to precisely how Congress ultimately believed it achieved that balance. If the language of the law is to have any meaning at all, then surely it must prevail over the kind of speculation that is entailed in such an enterprise as these courts have undertaken.

United States ex rel. Siller v. Becton Dickinson & Co., 21 F.3d 1339, 1354-55 (4th Cir. 1994), *cert. denied*, 115 S.Ct. 316 (1994).

CONCLUSION

The judgment of the Ninth Circuit should be reversed.

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Respectfully Submitted,

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